IN-DEPTH ANALYSIS
requested by the BUDG committee

The History of the EU Budget

Budgetary Affairs

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Abstract

The budget of the European Union has three pillars: its expenditure, its financing and its audit. This briefing looks at the origins of the budget, its development through multiannual planning and annual budgeting. It does so amid the European Parliament's changing powers over the budget, and the evolution of its financing and of the audit process. Since the very first European Community in 1952, there has been a tension over budgeting among the European institutions and the Member States, and a close link between reforms to expenditure and those to the financing.

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CONTENTS

LIST OF TABLES

LIST OF FIGURES

LIST OF ANNEXES

EXECUTIVE SUMMARY

In 1952, Europe's first political community for coal and steel was established with central, independent institutions that had a tax-raising power on the coal and steel sectors. This was beyond the direct control of the Member States. If the politics of the European Union's budget today are characterised by the reticence of national authorities to allow the Union to exercise budgetary activity, this is a tension that has lasted for nearly 70 years. After the 1960s the role of the Coal and Steel Community was diminished. The later Atomic Energy and Economic Communities, and the European Union that succeeded them, did not allow their central institutions to exercise direct tax-raising power.

This briefing analyses the budget-making powers of three European Communities that were founded in the 1950s. It explains how their budgets functioned, and the changes that occurred during the 1960s as the Communities were merged and as expenditure increased in new policy areas, notably the European Social Fund and in agriculture. This increase in expenditure created a tension between Member States with different priorities that was resolved by the Luxembourg Treaty of 1970. The solutions included a permanent financing base for the budget, and increased power of amendment and control of the budget by the European Parliament.

Expenditure increased further during the 1970s and 1980s with the introduction and later expansion of cohesion policy. From 1979, the European Parliament was emboldened by its direct election – before then it was appointed by national parliaments – and was in budgetary disagreement with the Council representing the Member States. As the internal market programme was launched in 1987, more investment would be needed and therefore a larger budget. Multiannual financial planning (or perspectives) removed some of the tension from the annual processes.

Next, the historic financing of the budget is addressed. This starts with the agreement on permanent financing of the budget concluded at the same time as the Luxembourg Treaty in 1970. As expenditure increased in the 1970s and 80s, there was increased tension on the financing side, as the British were dissatisfied with their budgetary imbalance. In 1984 the British were allocated a permanent "correction". Later, this led to the development of smaller "corrections" for other Member States. In 1988, the much larger future budget for the internal market required an increase in its financing, which was put in effect by drawing on a new resource based on each Member State's gross national product. Since then, the financing has fluctuated without major change other than a reduction in the use of value added tax and a concomitant increase in what is drawn from national wealth.

On the subject of audit, the roles of the audit institutions in the early Communities are addressed. In 1975, a Court of Auditors was established as an independent institution. It produces an annual report on the Union's accounts, and chooses to issue a "statement of assurance" if the accounts are in order. The European Parliament has, since 1979, possessed a specialist committee on audit that considers the annual accounts and reports from the Court of Auditors. It then prepares the Parliament's decision on whether to ratify the relevant year's accounts in a "discharge".

The final section defines some technical terms in the language of the budget. These comprise commitments, payments and RAL, differentiated and non-differentiated appropriations, pre-allocation and non-pre-allocation, and the significance of the "Gentleman's Agreement", and of the concept of "No budgetary lines without a legal basis".

A timeline of the budget's history appears in Annex I at the end of this briefing.

1. THE ORIGINS OF THE BUDGET

- How the original Communities' budgets operated
- The implications of merging the Communities
- The growth of the Communities' expenditure
- The budget treaties of the 1970s and the empowerment of the European Parliament over annual budgets

1.1 The European Coal and Steel Community, 1952

Europe's first political Community, the European Coal and Steel Community (ECSC), came into existence in 1952. Its role was to regulate the coal and steel industries in the six founding Member States (Belgium, France, Germany, Italy, Luxembourg, and Netherlands) and to create a single market for those products. The ECSC was governed by four central, integrated institutions:

- The High Authority, an executive, which was the predecessor of the European Commission
- A Council representing the Member States, chaired in rotation for periods of three months by one of the Member States
- An Assembly consisting of delegates from national parliaments, the predecessor of the European Parliament
- A Court to adjudicate in legal disputes

The High Authority exercised significant powers within the areas of coal and steel. These included managing the finances of the ECSC with independence. Unlike the later European Communities, the ECSC did not run on the basis of an annual budget. The ECSC was financed through a levy of a maximum of 1 percent of turnover of the coal and steel industries, tariffs on coal and steel imports, and fines equivalent to a maximum of 5 percent of turnover of affected enterprises. The High Authority set the levy within those limits, and this could only be blocked by a majority of four of the six Member States in the Council.

Finances raised through this real European tax, the levy, could be used for administrative expenditure by the ECSC's institutions (Article 78 ECSC) or on technical and economic research concerned with coal and steel (Article 55 ECSC). For re-adaptation of the coal and steel sectors (Article 56 ECSC), the ECSC could lend money, raised through loans on the financial markets (Article 51.1 ECSC), thus incurring debt, which was forbidden in later European treaties. Administrative expenditure was authorised by a unanimous "Committee of the Four Presidents" consisting of the Presidents of each of the four institutions, chaired by the President of the Court of Justice.

1.2 The Atomic Energy and Economic Communities, 1958

The European Atomic Energy Community (Euratom) and the European Economic Community (EEC) came into effect in 1958. These were led by institutions that still exist: the executive Commission, the Assembly (which has become the European Parliament), the Council representing the governments of the Member States, and the Court of Justice.

The budget for Euratom was divided into operational (administrative) and Research and Investment headings. The Euratom and EEC budgets had to be in balance – unlike that of the ECSC – and their procedures are the basis for the budget procedure that exists to this day: the Commission proposed an annual budget, the Assembly was consulted, and the Council decided (Article 171 Euratom; Article 199 EEC).

Since 1958, annually each institution and agency sent in estimates of their future financial needs during the first part of the year. The Commission proposed the next year's budget by September. The Council decided by a qualified majority vote (QMV)[1] of its members by October. The Assembly had a month to propose changes. The Council then made a final decision by QMV, or by unanimity depending on the policy area.

If a budget is not agreed before the beginning of the new year, monthly provisional budgets, or "provisional twelfths" took effect (Article 204 EEC) and this continues today (Article 315 TFEU).

Once the budget has passed, the Commission implements it. Article 179 Euratom and Article 209 EEC, just as their successor treaties, foresaw the passing of a Financial Regulation, a piece of ordinary legislation to establish the rules for administering the budget beyond what was specified in the treaties.

Finally, Article 180 Euratom and Article 206 EEC established an audit procedure and board of auditors (see section 4 of this briefing).

1.3 The Merger Treaty, 1967

In 1967, a merger treaty between the different European Communities took effect. This merged the High Authority into the European Commission, and created a single structure of European Parliament (EP), Council, Court of Justice, and Audit Board. The ECSC levy survived until 2002 and was decided by the European Commission, while the EP's right to be consulted on the Euratom and EEC budgets was extended to that of the ECSC (De Feo 2015a: 23). The ECSC's separate auditor survived until 1977. The administrative expenses of the ECSC were taken over by the European Community budget and the "Committee of the Four Presidents" was abolished. In 2002, the ECSC Treaty expired and financial arrangements for coal and steel fell fully within the European Union (EU) Budget.

Pressure for changes to the treaties on the budget occurred alongside the development of European expenditure policies. The ECSC and Euratom had investment budgets from the beginning. In 1958, the first EEC expenditure policy was launched, the European Social Fund (ESF), which invested in vocational training and re-insertion of the unemployed into the labour market.

The Common Agriculture Policy emerged as an area of expenditure in 1962 (De Feo 2015b: 30) to flank agricultural subsidies in other economies like that of the US. Emphasis was on production, with environmental concern and market orientation emerging only in later years. It was envisaged that agricultural expenditure would be financed through tariffs, approved only in 1970. Until then, fixed contributions from each Member State applied. The first funding period was multiannual from 1962 until 1965, when it was renewed for three more years. Pressure grew for a new treaty that could

[1] Each Member State had a certain number of votes according to its size. From 1958 to 2009, the threshold for a qualified majority, when unanimity does not apply, has varied between 67 and 74 percent of the votes. The changed threshold under the Lisbon Treaty is 55 percent of Member States, representing at least 65 percent of the EU's population. The votes per Member State in the 1960s are illustrated in Table 1.

guarantee long-term financing for agriculture (a demand of France) in exchange for greater control of the budget by the EP and openness to British membership of the Communities, which France conceded to the other members.

1.4 The Treaties of Luxembourg, 1970 and of Brussels, 1975

Until 1970, the EP had exercised only the right to be consulted about the budget, but was demanding the right to impose amendments. The treaties of Luxembourg and Brussels also coincided with the Community's first enlargement to Denmark, Ireland and the United Kingdom (UK), the decision to create Own Resources or permanent financing for the budget through tariffs and valued added tax (VAT) (see section 3), and the creation of the European Regional Development Fund to respond to the development needs of regions in Ireland, Italy and the UK.

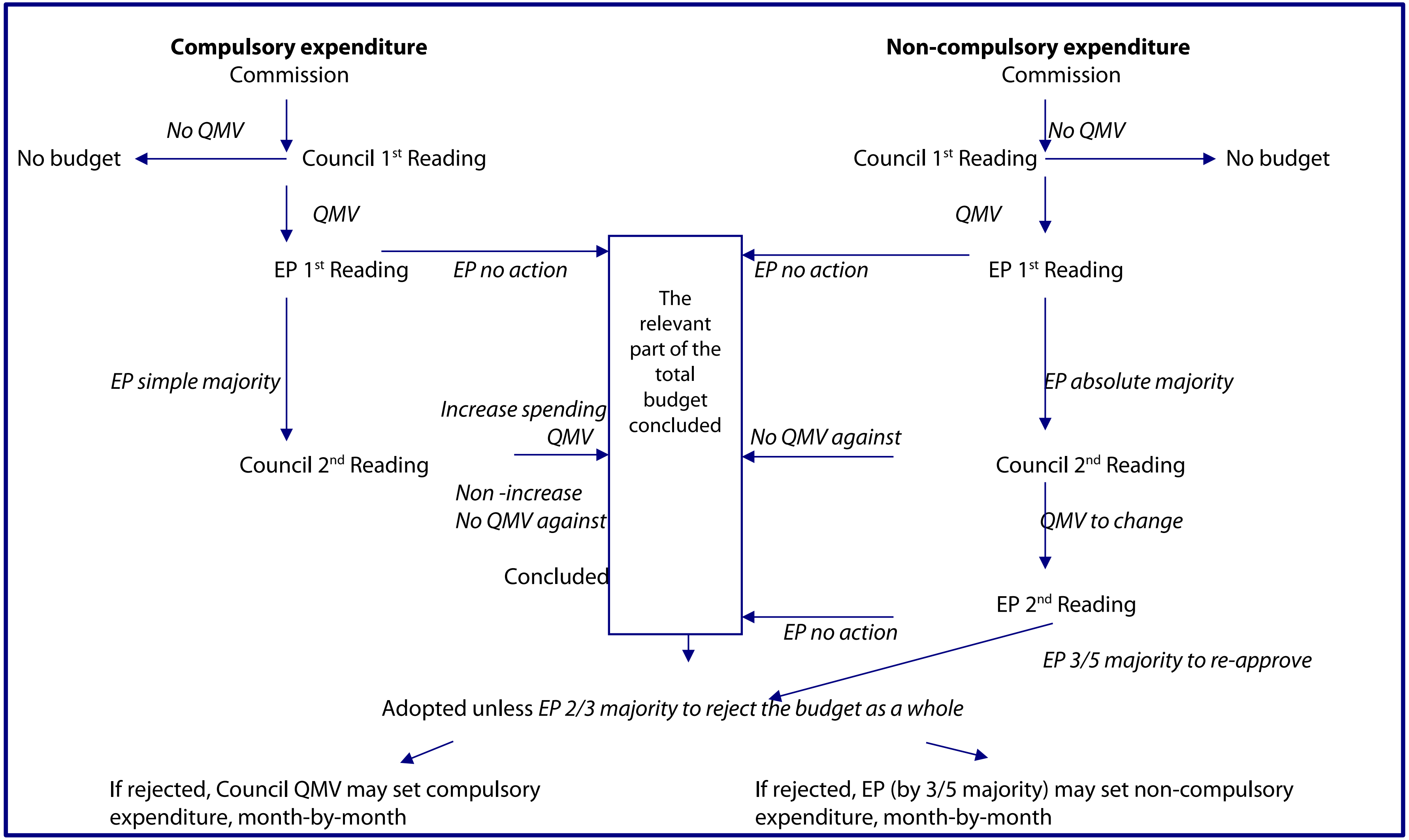
The treaty of 1970 divided expenditure into two types: compulsory expenditure (CE), which the Community was under a contractual obligation to pay due to its vague definition as 'expenditure necessarily resulting from this Treaty or from acts adopted therewith' (Article 272(4) EC), and everything else, which was deemed non-compulsory expenditure (NCE). Classifying expenditure as CE or NCE was the subject of dispute because each type of expenditure gave different powers to the Council or the EP. The European Court referred the question of definition back to the EP and Council for them to decide (European Parliament, Council and Commission 1982). Direct grants in agriculture and fisheries, and expenditure relating to international agreements were deemed part of CE, while nearly all else was NCE, a distinction that lasted until the Lisbon Treaty in 2009 (Benedetto and Høyland 2007).

Under the 1975 procedure (see Figure 1), the Council would vote by QMV. If the Council and EP disagreed, the Council would be able to impose its preference for CE on the EP, while the EP could do the same, overpowering the Council on NCE. In 1975, the EP gained the power definitively to reject the budget.

The treaties of 1970 and 1975 also transformed the audit powers of the Council and EP, and in 1977 turned the Audit Board into a Community institution, renamed the Court of Auditors (see section 4).

Finally, the treaty of 1970 allowed for the fixed Member State contributions to be replaced by Community-wide Own Resources, which would require the passing of a new legal act called the Own Resources Decision (for more on this see section 3).

Figure 1: The budgetary procedure of 1975



Source: Adapted from Benedetto and Høyland (2007).

2. FROM COMMON MARKET TO INTERNAL MARKET

- The elected Parliament and budgetary conflict
- Moving towards an internal market
- Multiannual financial planning
- Annual budgets and the Lisbon Treaty

In 1979 the first direct elections to the EP took place. There was now a larger budget, covering agricultural, social and regional development policies, backed by more solid financing through Own Resources (see section 3).

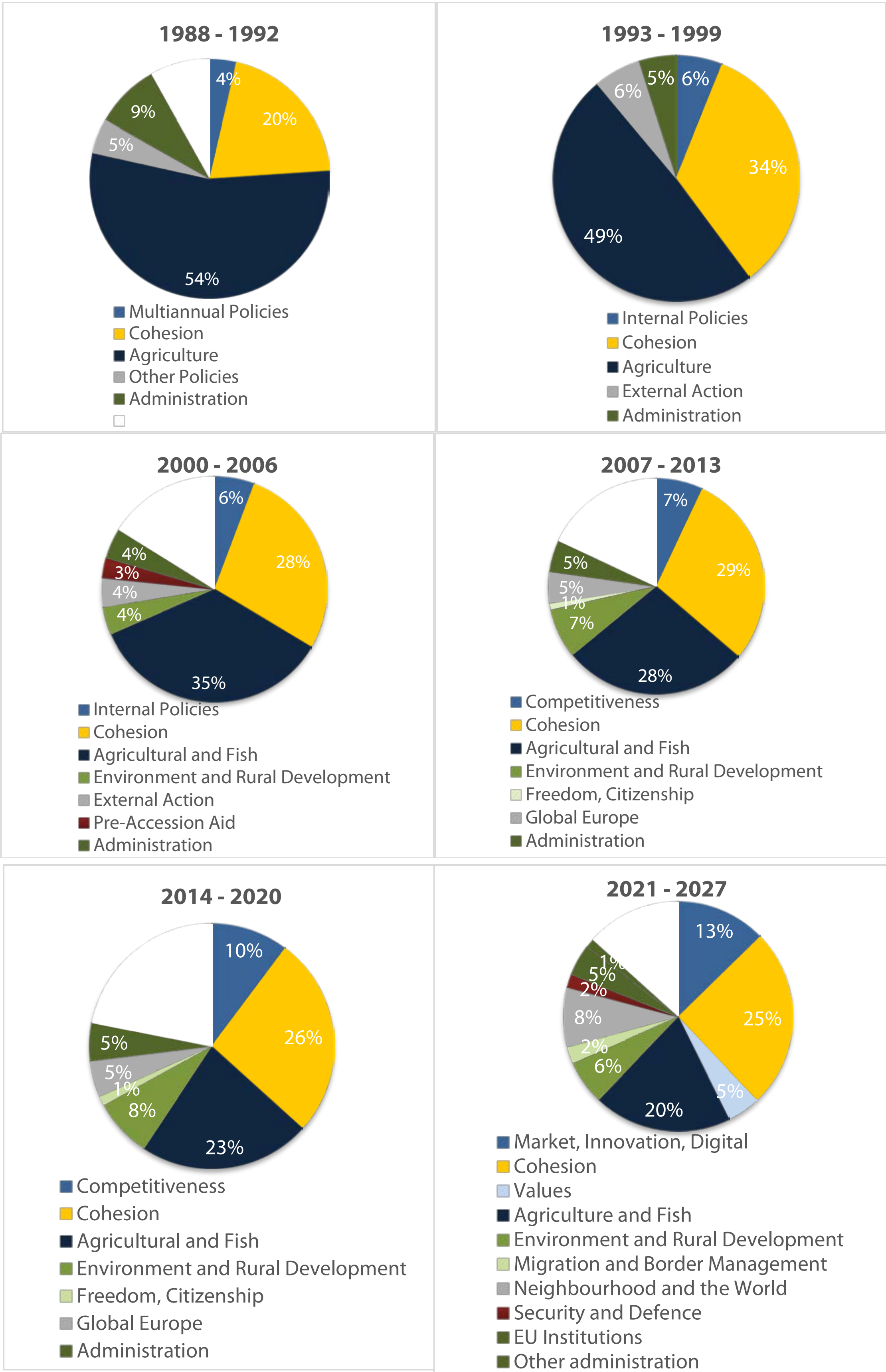
As the 1970s and 1980s progressed, the earlier agreement of 1970 began to break down. The elected EP demanded more influence – it initially failed to agree the budgets of 1980, 1985, 1986 and 1988 (De Feo 2017: 47). After non-agreement and resort to provisional monthly budgets, the annual budget for 1980 was approved seven months late. The budget of 1982 was adopted by the EP without Council agreement on NCE leading to a Court of Justice ruling that compelled the EP and the Council to negotiate over a definition of what was categorised either as CE or NCE (De Feo 2017: 49).

After ratification of the Single European Act in 1987, which created the Internal Market, the Commission brought forward plans for a new agreement between the Commission, the Council and the EP (known as an Interinstitutional Agreement) on a longer-term budget, or financial perspective (European Commission 1987). The consequence was an increase in the size of the budget, particularly for regional cohesion in Greece, Portugal and Spain, to prepare for the Internal Market. It introduced long-term planning, and made the budget more stable over periods of several years, so as to end the budget conflict of the 1980s between the EP and the Council. The package lasted from 1988 to 1992 (Figure 2 and Annex III).

2.1 Financial Perspectives and Multiannual Financial Frameworks from 1988

The first long-term financial perspective started in 1988. These were renamed as the Multiannual Financial Frameworks (MFF) in 2009 by the Lisbon Treaty, when the concept of the MFF was included in the treaties under Article 312 TFEU. These packages set maximum levels of expenditure, or ceilings. The real expenditure is delivered in the expenditure programmes like the ESF, with moneys disbursed in annual budgets. Procedurally, the Commission proposes the perspective or MFF. This would need agreement between the EP and a unanimous Council. Before 2009, it also need ratification in the national parliaments, now no longer required. If there is no agreement on a new multiannual expenditure programme as the old one is expiring, the pre-existing levels of expenditure roll over, even if expenditure programmes have expired. However, before 2009, either the Commission, or the Council, or the EP had the power to vote to end the multiannual programming and return to the situation of annual budgeting, as had been the case before 1988. The Lisbon Treaty since 2009 removes this power of sabotage. Failure to agree a new MFF means the previous one is destined to roll over.

Figure 2: Shares of expenditure since 1988 (baseline: commitments at 1.28% GNP in 1993-99)



Source: Annex II

Since 1988, how much has been spent? As Annex III shows, commitments, which are projected spending, grew in real terms from 1.00 percent of the EEC's collective wealth – gross national product (GNP) – to 1.20 percent in 1988 due to the decision to invest in the internal market programme, particularly in cohesion in the less developed regions. In 1993, this increased to 1.28 percent to allow for more investment in Cohesion during the preparation for the entry into force of the euro at the end of the 1990s, and in internal policies that include research and innovation (R&I). Preparing the old Member States for the growth in European Union (EU) membership in 2004, the next planning period that started in 2000 saw a real terms reduction in the budget to 1.08 percent of GNP. Amounts for internal policies like R&I, and for pre-accession aid were increased, while agricultural expenditure was reduced. Following the EU's enlargement of 2004, there was another expenditure reduction in 2007, which saw a small increase for "competitiveness" as most internal policies were renamed. Expenditure in the combined total for agriculture and rural development was reduced, and a new, barely financed heading for citizenship, freedom, security and justice, was introduced. In 2014, real terms expenditure was reduced further to 1.00 percent gross national income (GNI),[2] within which financing for competitiveness, in particular R&I, increased, while agricultural financing decreased.

The proposed figures for the funding period that starts in 2021 project an increase to 1.11 percent of GNI to take account of the effect of the UK leaving the EU. Competitiveness is renamed as a Single Market heading but loses the Erasmus+ programme to a new subheading called Values. Given the reallocation of Erasmus+ the rest of what was Competitiveness sees a significant increase in the proposal. Cohesion and agriculture are significantly reduced. In the light of the security and migration crises, the old headings for Citizenship, and for Global Europe (Foreign Policy) are reconfigured, with expenditure significantly increased under new headings for Migration and Border Management, [Europe's] Neighbourhood and the World, and Security and Defence. The figures reported in this paragraph are the basis of the Commission's proposal, and in May 2019 still subject to amendment and agreement by the Council and the EP.

Figure 2 illustrates the changing weights of each type of policy expenditure in percentage share since 1988. It uses the high level of commitments (spending projections) of 1.28 percent GNP in the 1993-99 period as a baseline. A total budget lower than 1.28 percent of GNP is a choice, which means that savings in one policy area are not being reinvested in another by the EU. For the other periods, percentage expenditure by policy is in proportion to the levels of 1993-99, with the "non-budget" appearing in white on the pie charts.

2.2 The Annual Budget and the Lisbon Treaty since 2009

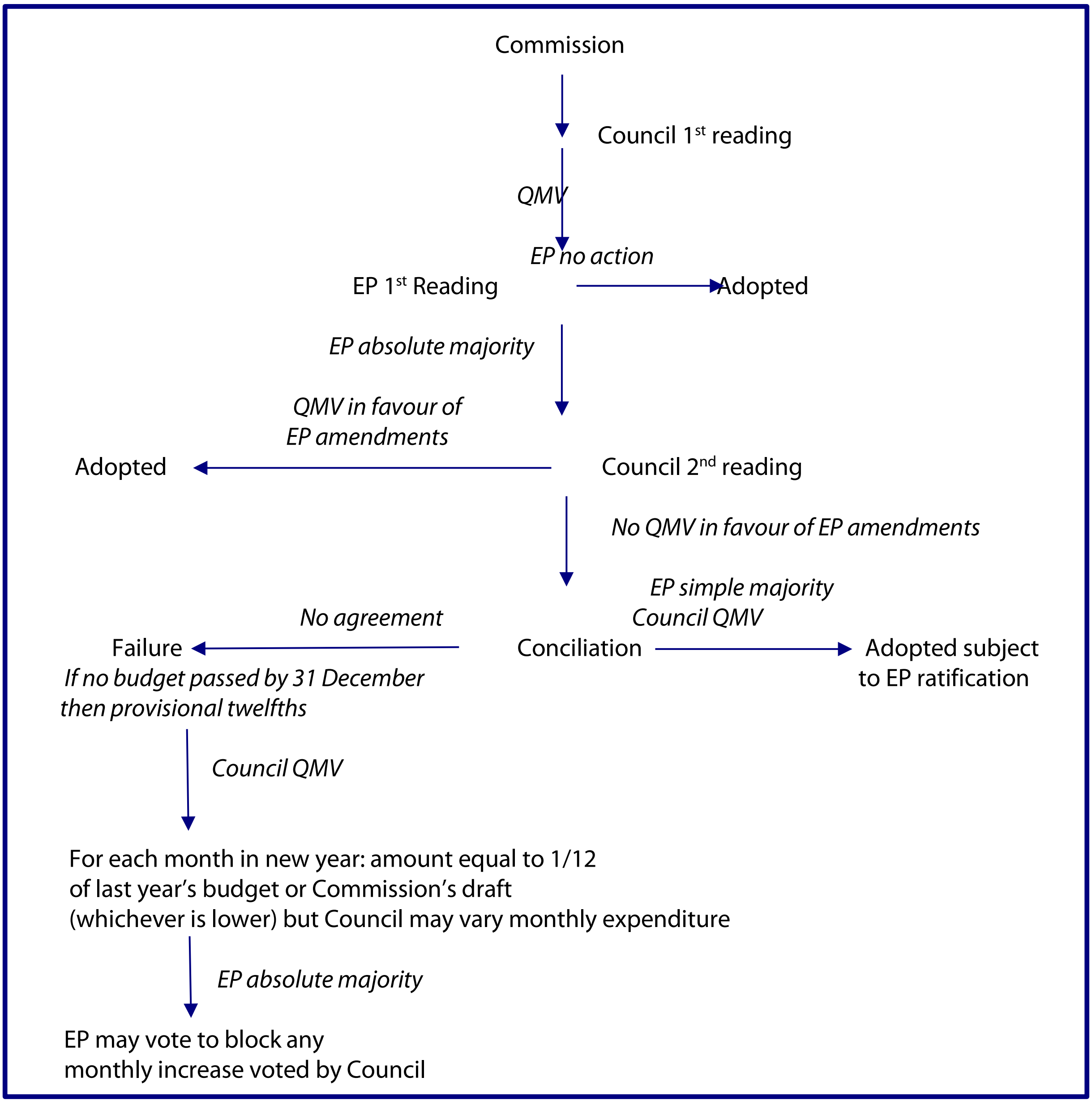
Since 2009, the annual budget procedure has changed significantly from that of the 1975 reported in Figure 1. The new procedure (Articles 314-315 TFEU) is illustrated in Figure 3. It is similar to the ordinary legislative procedure, in which the Council and EP decide together on most EU legislation, though it also has important differences. The life cycle of an annual budget is illustrated in Annex II.

The Commission proposes, the Council decides or amends by QMV, and the EP in turn may amend via an absolute majority of its membership. If the Council and the EP disagree, a conciliation committee composed of members of both institutions tries to agree a compromise. If there is no agreement in the conciliation committee within three weeks, the budget fails and the Commission may re-propose a

[2] GNI is a national accounting definition which is very similar to gross domestic product and GNP but with some corrections to better reflect relative wealth. GNI replaced GNP as the accounting definition for the size of the budget in 2007.

new one. If the conciliation committee agrees, its decision needs to be approved by the EP and the Council. There are some other unrealistic outcomes that are explained elsewhere (Benedetto 2013: 359).

Figure 3: The budgetary procedure after 2009



Source: Adapted from Benedetto and Høyland (2007)

If there is no agreement on a new budget by 31 December, provisional twelfths take effect in the new year. These are monthly budgets worth one-twelfth of either the previous year's expenditure or of that proposed by the Commission (whichever is lower). The Council may vary such expenditure. The EP, however, is limited only to blocking any increases. This makes it more likely that annual budgets in the future will be lower (Benedetto 2013) than otherwise. There are possible exceptions when the EP can use agreement on a new MFF to extract concessions from the Council. This is what happened in 2013 when the multiannual financing for 2014-2020 was negotiated. In exchange for its consent on the MFF, the EP secured slightly higher expenditure for the years 2013 and 2014, a concession of more flexibility in the MFF, and a review of the budget's Own Resources (Benedetto 2019).

3. OWN RESOURCES SINCE 1970

- How the budget is financed
- Permanent financing agreed in 1970
- The British "correction" and other corrections
- The return to national contributions through gross national income

3.1 Own Resources in the 1970s

Own Resources are the financing or revenue side of the budget, and their reform has often accompanied that of expenditure. The ECSC was from 1952 to 2002 financed by a levy on the turnover of the coal and steel industries. Euratom and the EEC were initially financed according to formulae in their treaties (Article 172 Euratom; Article 200 EEC) illustrated in Table 1. Contributions towards the ESF and the research programmes of Euratom were lower for Italy and the Netherlands, reflecting lower levels of wealth, than for the financing of other policies. Article 200 EEC allowed for these provisional rates to be replaced by real Own Resources, which were agreed in 1970 with a change to the treaty followed by the first Own Resources Decision (Council 1970). The content of the 1970 agreement and its successors is illustrated in Table 2. The share of each Own Resource in the financing of the Community and later EU is shown in Figure 4.

Table 1: Member State percentage contributions, and voting power, 1958-74

	BE	DE	FR	IT	LU	NL
CONTRIBUTIONS						
Administrative for EEC, Euratom 1958-70	7.9	28.0	28.0	28.0	0.2	7.9
EEC contributions to European Social Fund, 1958-70	8.8	32.0	32.0	20.0	0.2	7.0
Contributions for Euratom research, 1958-70	9.9	30.0	30.0	23.0	0.2	6.9
Transitional as own resources are introduced, 1971-74	6.8	32.9	32.6	20.2	0.2	7.3
VOTING POWER						
Votes per country towards a qualified majority of 12/17 until 1972	2	4	4	4	1	2
Votes per country for ESF decisions, 67/100 until 1972	8	32	32	20	1	7

Sources: (Articles 148, 200 and 203 EEC; Article 176 Euratom; Council 1970)

The budget was fixed at 1 percent of GNP. It was to be financed through agricultural and sugar levies, and by the external customs tariff. If these proved insufficient, the rest was to be made up from a call on VAT in the Member States. As the EEC Customs Union had taken effect in 1967, an external tariff already existed but was "owned" by the collecting Member State. This was now to be transferred to the European level but 10 percent of the value of the tariff was to be retained by the collecting Member State. The agreement was implemented between 1971 and 1974, with the gap until then being financed through proportions between countries reported in Table 1. From 1975, a call of 1.0 percent on the total VAT take was to be made available, implemented by 1977.

Table 2: Own Resources changes since 1970

1970	1985	1988	1994
External Tariff, Agricultural and Sugar Levies	External Tariff, Agricultural and Sugar Levies	External Tariff, Agricultural and Sugar Levies	External Tariff, Agricultural and Sugar Levies
Cost of 10% retained by collecting member state Incremental introduction 1971-74	Cost of 10% retained by collecting member state	Cost of 10% retained by collecting member state	Cost of 10% retained by collecting member state
VAT call rate of 1.0% from 1978, incremental 1975-77	VAT call rate from 1.0 to 1.4% in 1986, unanimous power to increase to 1.6% from 1988	VAT call rate remains at 1.4%	VAT call rate from 1.4 to 1.0% incrementally 1995-99
		VAT call rate capped when consumer spending exceeds 55% of a country's GNP	VAT call rate capped at 50% GNP for GR, ES, IE, PT from 1995, and for all others incrementally, 1995-99
	UK rebate worth 66% of UK net contribution financed by other members' VAT	UK rebate worth 66% of UK net contribution financed by other members' GNP shares	UK rebate worth 66% of UK net contribution financed by other members' GNP shares
	Rebate on the rebate of 33% for DE Lump sum of ECU 1bn paid to UK in 1985 from VAT share of other members	Rebate on the rebate of 33% for DE	Rebate on the rebate of 67% for DE
		GNP resource makes up the difference	GNP resource makes up the difference
		Commitments ceiling 1.30% GNP Payments ceiling 1.15% GNP in 1988 rising to 1.20% by 1992	Commitments ceiling 1.335% GNP Payments ceiling 1.21% GNP in 1995 rising to 1.27% GNP by 1999

Sources: Council (1970; 1985; 1988; 1994; 2000; 2007; 2014) and European Commission (2018a).

Table 2: Own Resources changes since 1970

2000	2007	2014	Proposal for post-2020 period
External Tariff, Agricultural and Sugar Levies Cost of 25% (increased from 10%) retained by collecting member state	External Tariff and Levies Cost of 25% retained by collecting member state	External Tariff and Levies Cost of 20% (reduced from 25%) retained by collecting member state	External Tariff and Levies Cost of 10% (reduced from 20%) retained by collecting member state
VAT call rate 1.0% in 2000-01, 0.75% in 2002-03, 0.5% from 2004 VAT call rate capped when consumer spend exceeds 50% of a country's GNP	VAT call rate reduced from 0.5% to 0.3%, but reduced to 0.225% for AT, 0.15% for DE, and 0.1% for NL and SE VAT call rate capped when consumer spend exceeds 50% of a country's GNI	VAT call rate 0.3%, but reduced to 0.15% for DE, NL, SE VAT call rate capped when consumer spend exceeds 50% of a country's GNI	Vat call rate 0.3%, increased for DE, NL and SE based on real VAT resource
UK rebate worth 66% of UK net contribution financed by other members' GNP shares, excluding the effect of pre-enlargement expenditure in post-2004 Member States Rebate on the rebate of 75% for DE, AT, NL, SE	UK rebate worth 66% of UK net contribution financed by other members' GNI shares, excluding the effect of pre-enlargement expenditure in post-2004 Member States Rebate on the rebate of 75% for DE, AT, NL, SE Annual lump sum rebates to NL of €605M and to SE of €150M, funded by all member states from GNI	UK rebate worth 66% of UK net contribution financed by other members' GNI shares, except with regard to non-agricultural expenditure in post-2004 Member States Rebate on the rebate of 75% for DE, AT, NL, SE Annual lump sum rebates to DK of €130M, NL of €695M, to SE of €185M. For AT, total lump sum of €60M, funded by all member states by GNI	UK rebate abolished by Brexit. Lump sum rebates for AT, DE, DK, NL, SE phased out 2021-25 3% call rate on Common Consolidated Corporate Tax Base 20% revenue from European Emissions Trading System Levy of €0.80 per kilo of non-recycled plastic packaging
GNP resource makes up the difference	GNI resource makes up the difference	GNI resource makes up the difference	GNI resource makes up the difference
Commitments ceiling 1.335% GNP Payments ceiling 1.27% GNP	Commitments ceiling 1.31% GNI Payments ceiling 1.24% GNI	Commitments ceiling 1.29% GNI Payments ceiling 1.23% GNI	Commitments ceiling 1.35% GNI Payments ceiling 1.29% GNI

The Commission and the EP had proposed for the EP to have real power to influence the introduction of and changes to Own Resources in 1970 and in 1975, for the EP to be able to consent to the ECSC levy, and for the EEC to have the power to issue debt (Benedetto 2017: 619) but the Council did not accept these. The EP has tried to influence Own Resources ever since, but without luck unless it could link reform to other questions (Benedetto 2019; Lindner 2006). Own Resources continue to be passed or modified only if the Council agrees unanimously, followed by EP consultation, and ratification in every national parliament (Article 311 TFEU).

3.2 The British Rebate at Fontainebleau, 1984

By 1984, the Community was drawing on the external tariff and on VAT up to its maximum call rate of 1.0 percent, yet the budget was insufficient to meet previous commitments. The UK demanded that its budgetary imbalance be addressed and was in a position to block any decision that required unanimous agreement, including increasing the size of the VAT call rate or accepting Community enlargement to Portugal and Spain.

A package was agreed at Fontainebleau in 1984 (Council 1985), in which the UK gained but also made concessions. The UK gained a "correction" worth two-thirds of the size of its net contribution, and a single payment of 1 billion ecu in 1986. This was financed by the other Member States through their VAT shares until 1987, though West Germany's contribution to the UK was discounted by one-third.[3] In exchange, the UK accepted an increase in the VAT call rate from 1.0 to 1.4 percent from 1986 and the Community's enlargement to Portugal and Spain (Benedetto 2017: 623).

3.3 Own Resources and the Internal Market

Agreement on the Single European Act led to the long-term financial perspectives for expenditure. On the revenue side, a new decision was reached four years after Fontainebleau to finance the increased expenditure (Council 1988).

For the first time, a ceiling for Own Resources as well as expenditure was agreed, so as to contain this larger budget. Absolute Own Resources available for all EU obligations could be no larger than 1.30 percent of GNP, providing real cash (payments) of 1.15 percent GNP in 1988, rising to 1.20 percent by 1992. The VAT take was also capped for those countries whose consumer expenditure represented more than 55 percent of their GNP. This compares with a multiannual ceiling for expenditure commitments at 1.20 percent GNP and payments at 1.15 percent, during the same time period.

The increase in size of the budget in 1988, and the effective reduction of the VAT resource, meant that there was a shortfall. The 1988 agreement is most important for introducing the GNI resource. Once income from tariffs, levies and VAT was exhausted, the "residual" or remaining difference was made up from an equal share of each Member State's GNP.

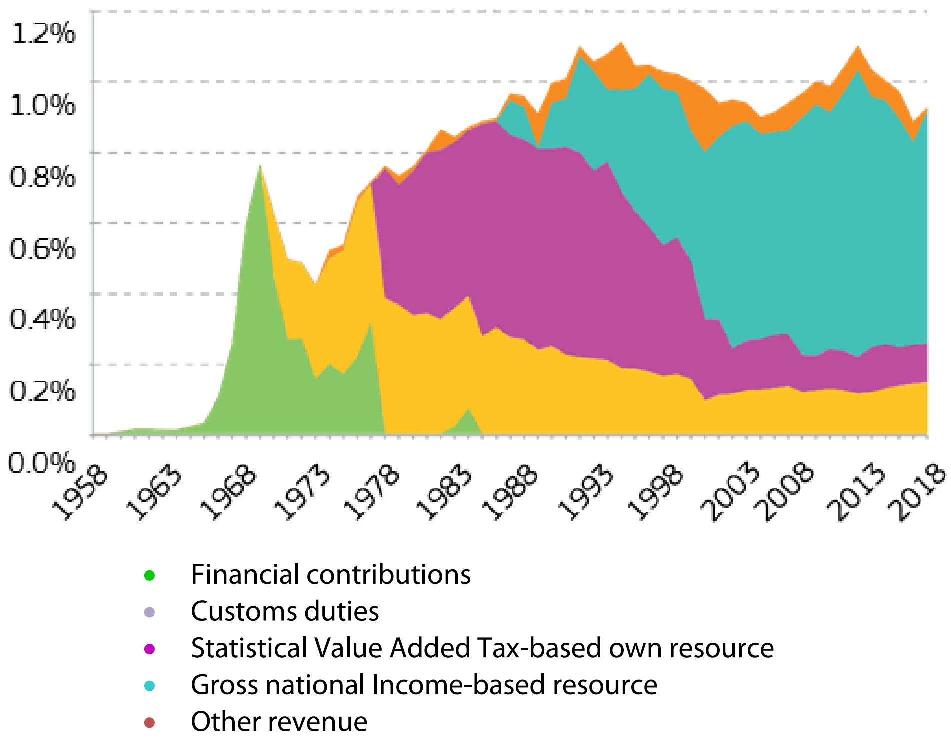
At the beginning of the next financial perspective, a new Own Resource Decision was reached (Council 1994). To support higher expenditure on the internal market and preparation for the euro, the maximums (ceilings) for projected expenditure (commitments) increased from 1.30 to 1.335 percent of GNP, while

[3] Since 1985, the UK "correction" has evolved as illustrated in Table 2. The UK does not benefit from the size of the EU's non-agricultural expenditure in Member States that have joined since 2004.

those for payments increased from 1.20 to 1.27 percent in increments until 1999. The VAT share underwent a significant reduction, capped for countries where consumer expenditure exceeded 50 percent of GNP in the case of Greece, Spain, Ireland and Portugal from 1995 and for others from 1999. The VAT call rate was also reduced incrementally from 1.4 to 1.0 percent by 1999. Given the larger budget and fall in VAT, more money was sourced "to make up the difference" from each Member State's GNP. The size of Germany's discount from the UK rebate increased from one-third to two-thirds.

The Own Resources Decision to take account of eastern enlargement and the financial programming from 2000 (Council 2000) retained the resources ceilings and the UK "correction". As the UK had grown economically, richer Member States demanded abolition of the "correction" or the right to have ones of their own. A hidden "correction" for the Netherlands, home of Europe's largest commercial port, was the decision to increase the "cost" retained by countries for collecting the external tariff from 10 to 25 percent. The UK "correction" was unchanged, apart from the UK not benefiting after the 2004 enlargement from the equivalent of pre-accession aid granted to the new Member States. In terms of the financing of the UK's "correction", Germany's discount increased from 67 to 75 percent, and was also extended to Austria, the Netherlands and Sweden. Finally, the VAT call rate was halved from 1.00 to 0.75 in 2002 and then to 0.50 percent from 2004. Given the unchanged maximum in Own Resources, these reductions in financing led to an increase on the amount made up from each Member State's GNP (Figure 4, see also Table 2).

Figure 4: Evolution of Own Resources since 1958



Source: European Commission (2018a).

Following the EU's enlargement and lower spending ceilings agreed in the financial perspective of 2007-2013, the 2007 Own Resources Decision (Council 2007) reduced the Own Resources ceilings in projected revenue from 1.335 to 1.31 percent GNI, and for real payments from 1.27 to 1.24 percent GNI.[4] The VAT call rate was reduced from 0.5 to 0.3 percent, though reduced further for Austria at 0.225 percent, Germany at

[4] The budget and Own Resources were calculated in GNI rather than GNP from 2007.

0.15 percent and the Netherlands and Sweden at 0.10 percent, as part of a "correction" for those countries. Moreover, annual lump sum "corrections" were paid of €605 million to the Netherlands and €150 million to Sweden, financed by all the Member States through their GNI. The reduction of the VAT resource led to an increase on what was drawn from each Member State's gross national income (Figure 4).

A reduction in expenditure in the MFF of 2014-2020 led to a fall in the Own Resources ceilings in the Decision of 2014 (Council 2014). These were reduced for projected resources (commitments) from 1.31 to 1.29 percent GNI, and for payments from 1.24 to 1.23 percent GNI. The collection "costs" retained for collecting the external tariff were reduced from 25 to 20 percent. The VAT call rate remained 0.3 percent, increasing for Austria from 0.225 percent. For the Netherlands and Sweden it increased from 0.10 percent to 0.15 percent, which applied also to Germany. Annual lump sums were paid to the Netherlands of €695 million, to Sweden of €185 million, and newly to Denmark of €130 million. Austria, instead, received an amount of €60 million in 2016 only. These amounts were paid by all Member States.

The UK "correction" maintained its formula, but excluded from it was the value of non-agricultural expenditure in Member States that had joined since 2004. Austria, Germany, Netherlands and Sweden continued to receive a reduction on their contributions to the UK "correction".

After 2020 and the abolition of the UK's "correction" through Brexit, the European Commission (2018a) has proposed a reduction in the collection costs of the external tariff to 10 percent, a 0.3 percent call rate on VAT for all Member States, and temporary lump sum rebates for Austria, Denmark, Germany, Netherlands and Sweden that will be phased out by 2025. It has also proposed three new Own Resources building on the report of the High Level Group on Own Resources (Monti *et al.* 2017): a 3 percent call rate on a Common Consolidated Corporate Tax Base, a 20 percent share of revenue generated from the European Emissions Trading System, and a levy of €0.80 for every kilogram of non-recycled plastic packaging waste. It is projected that these three new Own Resources would raise around 10 percent of the financing needed for the EU budget. This proposal will need to be approved unanimously by the Council, and then by the national parliaments of the Member States.

4. AUDITING THE BUDGET

- The Coal and Steel Auditor and the Audit Board of Euratom and the EEC
- The Court of Auditors, Annual Report and Statement of Assurance
- The European Parliament's Budgetary Control Committee
- Discharge

An audit process for the Community and EU budgets existed since the ECSC Treaty in 1952. An auditor was appointed by the Council for a three-year term (Article 78.6 ECSC), who would then account to the "Committee of the Four Presidents", which contained the Presidents of each of the four ECSC institutions. The High Authority would report annually on its accounts to the Council.

Euratom and the EEC from 1958 had an Audit Board. The Council unanimously decided on the number of auditors, and their appointment for a five-year term, including that of its chairman. The Board would inspect the accounts and produce a report on the budgets for each financial year. After this, the Council by QMV would grant "discharge" to approve that year's expenditure after the event and inspection of the accounts (Article 180 Euratom; Article 206 EEC).

The Luxembourg Treaty of 1970 extended some audit power to the EP by granting it and the Council a joint power of discharge over the budget (Articles 3, 6 and 9, Traité 1970).

The Brussels Treaty of 1975 reduced the Council's influence to "recommending" the discharge, which the EP would then decide (Articles 9, 17 and 25, Treaty 1975). More significantly, it transformed the Audit Board and the ECSC Auditor into a new independent institution, the European Court Auditors. It was to have nine members, *de facto* the same number as Member States, which increased as more countries joined. The Treaty of Nice in 2003 specified that there would be one auditor per Member State. They were appointed unanimously– or by QMV from 2003 – for a six-year term after consulting the EP and could from 1977 elect their own President.

In 1979, the EP became directly elected. In matters of audit, it established a Budgetary Control Committee separate from its Budgets Committee. The new committee took the initiative of preparing separate discharge votes on each of the Community's institutions and agencies, which challenges the Council's view that there should be only one discharge (Benedetto *et al.* 2017).

The Court of Auditors prepares an annual report on each year's budget having received accounts from the European Commission. It may examine assets, revenue and liabilities of the EU, with the power to audit EU expenditure at national level. Since 1993, the Court also has the power to issue a "statement of assurance" that the accounts of the EU are reliable (Articles 45c and 188c TEU). Since 2003, "this statement may be supplemented by specific assessments for each major area of Community activity" (Articles 45c, 160c and 248 TEU). Since 1999, the Court's remit goes beyond verifying the soundness of accounts to reporting on cases of irregularity (Articles 45c, 160c and 188c TEU). Since 1993, beyond financial compliance, the Court also draws up special reports on the quality of expenditure policies.

The life cycle of an annual budget through its agreement and audit stages is reported in Annex II.

5. FURTHER CONCEPTS

- Commitments, Payments and RAL
- Differentiated and non-differentiated appropriations
- Pre-allocation and non-pre-allocation
- The Gentleman's Agreement
- No budgetary lines without a legal basis

Some of the technical terms in the language of the EU's budget are explained in this section. A full glossary of terms is available here: https://ec.europa.eu/info/files/glossary_en

5.1 Commitments, Payments and RAL

The concept of commitments and payments can first be found in the Euratom Treaty, Article 176. They became a reality in the financial perspectives and Own Resources Decision since 1988, and a form of double-budgeting. The rules are set out in the Financial Regulation (Articles 7 and 12, European Parliament and Council 2018). The EU commits itself to invest over a number of years. The full commitments are entered in the budget in the year they are made. As projects are launched, some payments follow immediately, others following in future years as conditions are met and local co-financing is put in place. Payments can follow two to three years later, a concept known as *n+2* or *n+3*. Conditions are rarely met in full and so payments are almost always below the level of commitments. The accumulated difference in the amounts between commitments and payments is known as ***reste à liquider*** **(RAL).**

5.2 Differentiated and non-differentiated appropriations

Most expenditure aside from agricultural direct payments and EU administration is differentiated. This means that local or national co-funding is usually supplied to match financial commitments made by the EU over a number of years. In the case of agriculture and administration, which are non-differentiated, there is no local co-funding and the EU pays the full amount. In this case, payments closely follow commitments.

5.3 Pre-allocation and non-pre-allocation

In the context of the MFF and the legal acts agreed alongside it, each Member State is pre-allocated sums for agriculture and cohesion. Most other expenditure is non-pre-allocated meaning that eventual recipients will have had to compete in order to qualify for funds. The largest area of expenditure which is non-pre-allocated falls under the Competitiveness heading.

5.4 The Gentleman's Agreement

This is a political agreement between the EP and the Council that in the annual budget, they do not touch each other's administrative budgets. It dates back to 1970 and has been challenged in recent years on two counts. The first is that the non-law-making competences of the Council have grown, that it is also an executive, and that it may act in the EU's foreign policy, while the EP is merely a law-making institution. It is therefore justified for the EP to exercise a power of amendment over the Council's budget, but the Council still should not target the EP's internal budget. The second is that the Council has resisted full

scrutiny of its expenditure by the EP's Budgetary Control Committee. This has been the subject of a briefing and an investigation by the Budgetary Control Committee
(Benedetto *et al.* 2017).

The Council attached the following resolution to the 1970 treaty:

'The Council undertakes to make no amendments to the estimate of expenditure of the European Parliament. This undertaking shall only be binding in so far as this estimate of expenditure does not conflict with Community provisions, in particular with regard to the Staff Regulations of officials and Conditions of Employment of other servants, and to the seat of the institutions.' (Single European Act 1987: 1091).

In response to a parliamentary question from Hans-Peter Martin MEP in 2010, the Council clarified that: 'This resolution has always been interpreted and applied by the EP and by the Council to mean that each institution refrains from questioning the administrative budget of the other.' (European Parliament 2010).

5.5 "No budgetary lines without a legal basis"

During the 1970s, the ability of the EP or the Council to create new lines in the budget for expenditure that had no accompanying act or specific treaty article to establish it was disputed. The EP took the position that anything passed in the annual budget is automatically a legal basis, and so created 15 new lines in the budget of 1978 (De Feo 2015b: 71). The Council and Commission also created new lines. A ruling by the Court of Justice annulled budget lines that had been agreed without a legal base (European Court 1998). The dispute was solved by an agreement on legal bases and implementation of the budget, which is included in the Financial Regulation of the EU, of which the most recent version is that of 2018 (European Parliament and Council 2018: Article 59). Without a separate legal act, this allows for three types of line in the budget. Firstly, pilot projects to test feasibility for something that could develop, limited to two years at no more than €50 million per year. The Erasmus programme was born in the 1980s as a pilot project. Secondly, preparatory actions, which are to prepare future initiatives, and may last for three years though a legal act is needed by year 3. Thirdly, autonomous actions, which concern the administrations of the institutions.

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ANNEXES

Annex I: EU Budget Timeline

1952: European Coal and Steel Community founded. Financed by levy on coal and steel turnover.

1958: European Atomic Energy and Economic Communities founded. Annual budgeting, with specific roles for Commission, Council, Parliament and Audit Board. Financed by national contributions. European Social Fund launched. Council can approve accounts by granting discharge to the budget.

1962: Agricultural financing commences.

1967: Communities merge with single budget procedure.

1970: Parliament gains final say over non-compulsory expenditure in the budget. Own Resources are established to finance budget through tariffs and value added tax (VAT). Council and Parliament jointly grant discharge to the budget. Gentleman's agreement that Council and Parliament do not touch each other's internal budgets.

1975: European Regional Development Fund established.

1977: Parliament gains the power to reject the budget. Council and Parliament co-granting of the discharge replaced by Parliament doing so alone. European Court of Auditors replaces Audit Board and ECSC Auditor.

1978: "No budgetary line without legal base" evolves as a dispute, heard in Court in 1998, and solved by the Financial Regulation.

1979: First direct elections of the European Parliament. Parliament rejects budget of 1980, establishes Budgetary Control Committee, and passes discharges for each institution and agency, rather than a single discharge for the entire budget.

1984: Council at Fontainebleau approves "correction" for UK and increase in VAT call rate.

1988: Interinstitutional Agreement on long-term financial perspectives, including increase for regional development/cohesion. Own Resources Decision that reduces reliance on VAT and introduces contributions based on gross national product.

1993: Court of Auditors gains new power to grant or refuse a Statement of Assurance to confirm that EU annual accounts are in order.

1998: Court of Auditors' refusal to grant Statement of Assurance for the accounts of 1996 leads to the European Parliament refusing discharge and in March 1999 to the resignation of the Commission.

2006: European Parliament rejects new financial perspectives to secure its policy preferences before approval.

2009: Lisbon Treaty enters into force with most significant changes to the budget's rules since 1977. Conciliation process for annual budget means that budgets for 2011, 2013, 2015 and 2019 are agreed late.

Annex II: Life Cycle of Annual Budget and its Discharge, example of the 2019 Budget

January-March 2018: Parliament's Budgets Committee prepares guidelines for the 2019 Budget

April 2018: Commission receives estimates of 2019 spending needs from its own services and from all other institutions and agencies.

June 2018: Commission proposes 2019 Budget in advance of legal deadline of 1 September.

July 2018: Parliament's Budgets Committee prepares mandate for the 2019 Budget

September 2018: Council adopts its Common Position on the 2019 Budget.

September-October 2018: Parliament's Budgets Committee and then Plenary adopt amendments.

October-November 2018: Conciliation Committee sits for three weeks but unable to reach agreement, budget fails.

December 2018: Budget for 2019 rapidly re-proposed by Commission and adopted by Council and Parliament.

Year 2019: Budget implemented. Amending budgets adopted as circumstances change.

May 2020: Commission presents accounts for 2019.

May-October 2020: Court of Auditors examines accounts for 2019.

November 2020: Court of Auditors publishes Annual Report for 2019, and grants (or not) the Statement of Assurance.

November 2020-January 2021: Budgetary Control Committee of Parliament holds hearings with Commissioners, and assesses Annual Report of Auditors and Statement of Assurance for 2019.

January-February 2021: Council votes by QMV on recommendation of discharge.

February 2021: Parliament's Budgetary Control Committee prepares discharge resolution.

March 2021: Parliament decides on discharge for 2019, either 1) to grant, or 2) to refuse, or 3) to delay for six months pending further enquiries.

October 2021: If delayed, Parliament must decide to grant or to refuse discharge for 2019.

Annex III: Multiannual expenditure commitments since 1988

1988-1992 (prices of 1988)	Total (ECU mn)	Average Annual (ECU mn)	% spend	Baseline % of 1.28% GNP	1993-1999 (prices of 1992)	Total (ECU mn)	Average Annual (ECU mn)	% spend	Baseline % of 1.28% GNP
Multiannual Policies	9310	1862	3.8	3.6	Internal Policies	31587	4512	6.0	6.0
Cohesion	53140	10628	21.7	20.4	Cohesion	176398	25200	33.3	33.3
Agriculture	142200	28440	58.1	54.5	Agriculture	255570	36510	48.2	48.2
Other Policies	12488	2497.6	5.1	4.8	External Action	32400	4629	6.1	6.1
Administration	22700	4540	9.3	8.7	Administration	25480	3640	4.8	4.8
Commitments	244578	48916			Commitments	529885	75698		
Payments	234679	46936			Payments	505238	72177		
Commitments %GNP	1.20				**Commitments %GNP**	**1.28**			
Payments %GNP	1.15				Payments %GNP	1.22			
"Non-budget" due to Commitments at less than 1.28% GNP	16305			6.3	"Non-budget" due to Commitments at less than 1.28% GNP	0			0
Commitments if at 1.28 percent GNP	260883				Commitments if at 1.28 percent GNP	529885			

Sources: European Parliament, Council and Commission (1988; 1993; 1999; 2006), Council (2013), European Commission (2018b)

2000-2006 (prices of 1999)	Total (€ mn)	Average Annual (€ mn)	% spend	Baseline % of 1.28% GNP	2007-2013 (prices of 2004)	Total (€ mn)	Average Annual (€ mn)	% spend	Baseline % of 1.28% GNI
Internal Policies	43830	6261	6.8	5.7	Competitiveness	74098	10585	8.6	7.0
Cohesion	213010	30430	33.0	27.8	Cohesion	308041	44006	35.6	29.2
Agricultural and Fish	267370	38196	41.4	34.9	Agricultural and Fish	293105	41872	33.9	27.8
Environment and Rural Development	30370	4339	4.7	4.0	Environment and Rural Development	78239	11177	9.0	7.4
Pre-Accession Aid	21840	3120	3.4	2.9	Freedom, Citizenship	10770	1539	1.2	1.0
External Action	32060	4580	5.0	4.2	Global Europe	49463	7066	5.7	4.7
Administration	33660	4809	5.2	4.4	Administration	49800	7114	5.8	4.7
Commitments	646190	92313			Commitments	864316	123474		
Payments	641500	91643			Payments	820780	117254		
Commitments %GNP	1.08				Commitments %GNI	1.05			
Payments %GNP	1.07				Payments %GNI	1			
"Non-budget" due to Commitments at less than 1.28% GNP	119665			15.6	"Non-budget" due to Commitments at less than 1.28% GNI	189326			18.0
Commitments if at 1.28 percent GNP	765855				Commitments if at 1.28 percent GNI	1053642			

2014-2020 (prices of 2011)	Total (€ mn)	Average Annual (€ mn)	% spend	Baseline % of 1.28% GNI	2021-2027 (prices of 2018)	Total (€ mn)	Average Annual (€ mn)	% spend	Baseline % of 1.28% GNI
Competitiveness	125614	17945	13.1	10.2	Market, Innovation, Digital	166303	23758	14.7	12.7
Cohesion	325149	46450	33.9	26.5	Cohesion	330642	47235	29.1	25.3
					Values	61332	8762	5.4	4.7
Agricultural and Fish	277851	39693	28.9	22.6	Agriculture and Fish	254247	36321	22.4	19.4
Environment and Rural Development	95328	13618	9.9	7.8	Environment and Rural Development	82379	11768.	7.3	6.3
Freedom, Citizenship	15686	2241	1.6	1.3	Migration and Border Management	30829	4404	2.7	2.4
Global Europe	58704	8386	6.1	4.8	Neighbourhood and the World	108929	15561	9.6	8.3
					Security and Defence	24323	3475	2.1	1.9
Administration	61629	8804	6.4	5.0	EU Institutions	58547	8364	5.2	4.5
					Other administration	17055	2436	1.5	1.3
Commitments	959988	137141			Commitments	1134583	162083		
Payments	908400	129771			Payments	1104803	157829		
Commitments %GNI	1				Commitments %GNI	1.11			
Payments %GNI	0.95				Payments %GNI	1.08			
“Non-budget” due to Commitments at less than 1.28% GNI	268797			21.9	“Non-budget” due to Commitments at less than 1.28% GNI	173765			13.3
Commitments if at 1.28 percent GNI	1228785				Commitments if at 1.28 percent GNI	1308348			

The budget of the European Union has three pillars: its expenditure, its financing and its audit. This briefing looks at the origins of the budget, its development through multiannual planning and annual budgeting. It does so amid the European Parliament's changing powers over the budget, and the evolution of its financing and of the audit process. Since the very first European Community in 1952, there has been a tension over budgeting among the European institutions and the Member States, and a close link between reforms to expenditure and those to the financing.